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Thursday, October 4, 2001

UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

In re




DONALD O. GRACE,

No. 01-11078

[Debtor](#)  (s).

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### **Memorandum re Tax Returns**

In this [Chapter 7](#)  case, [creditor](#)  Robert Prior and the [trustee](#)  seek to examine certain income tax returns of Megann Grace Sanchez, daughter of debtor Donald Grace. The trustee alleges that Grace gave Sanchez funds in 1999 which were used to purchase property in Willow Creek. Sanchez' tax returns could contain evidence either substantiating Grace's version of the facts or indicating that his payments are avoidable as preferences or fraudulent conveyances. Sanchez argues that her tax returns are absolutely privileged.

There is no federal privilege protecting tax returns. California is one of a few states in which tax returns are privileged. [Sav-On Drug Stores v. Superior Court](#) (1975) 15 Cal.3d 1, 6. However, the privilege is only applicable in federal court to cases based on California law. [Lewis v. United States](#), 517 F.2d 236, 237 (9<sup>th</sup> Cir. 1975). The privilege is not applicable here because the information sought is pertinent primarily to federal bankruptcy issues.

Nonetheless, a federal court should still consider a state privilege in fashioning a remedy. 12 Fed.Proc.L.Ed., Evidence § 33:274. The court will accordingly order the production of the requested tax returns within ten days after entry of an appropriate order, but will allow Sanchez to redact therefrom any information not directly or indirectly related to payments

from Grace or to the Willow Creek property. Sanchez is warned that overzealous use of the power to redact will result in denial of the privilege altogether. Counsel for Prior shall submit an appropriate form of order.

Dated: October 4, 2001

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Alan Jaroslovsky

U.S. [Bankruptcy Judge](#) 

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